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ISSUE

¶1. Summary. Each week, Embassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:

- SNO Needs R9 Billion to Start;
- Growth in 2006 GDP May Slow as Consumer Demand Eases;
- Will the Rand Stabilize?;
- SA's Major Banks Increase Market Share;
- SA, China Close to Agreement to Limit Textile Imports; and
- Land Restitution Spending Increases

End Summary.

SNO Needs R9 Billion to Start

¶2. The second national telephone operator (SNO) licensed earlier in December will need a capital investment of about R9 billion ($1.4 billion, using 6.3 rands per dollar) before it can start commercial operations planned for the third quarter 2006, according to a recent Merrill Lynch study. Although details of the funding are still being discussed, the SNO's 26% strategic equity partner, Tata Holdings, has already spent R1.5 billion ($240 million) while parastatals Eskom Telecommunications and Transtel, which own 15% each in the SNO, have spent R2 billion ($320 million) on network capital expenditure. Black economic empowerment firm Nexus, which at 19% holds the second-biggest stake in the SNO, would have to fund all or part of the remaining R5.5 billion ($873 million). The Independent Communications Authority of South Africa issued the SNO with a 25-year renewable license to provide public-switched telecommunications services to about 14 specific areas. The second operator will use Telkom's network for a period of two years after its launch. Telkom will also have monopoly of the local loop for at least two more years after the launch of the second operator. Whereas Telkom's operating license requires it to provide a service to every person in South Africa who requests it, the SNO is obliged only to make services available to the 14 network service areas. The second operator, which still does not have a name, is required to ensure availability of services to 50% of the population within the 14 network areas in the next five years. It also has to ensure that 80% of the entire South African population can access its services after 10 years. Other license requirements include providing high-speed internet connectivity to at least 2,500 schools and 2,500 rural

clinics. Merrill Lynch forecasted that because of delays in the launch of the SNO, it would take only 2.5% of Telkom's market share by 2007, down from the bank's initial estimate of 4%. Telkom had projected that it might lose 10%-15% of its market share to the second operator in the next five years. Source: Business Day, December 27.

Growth in 2006 GDP May Slow as Consumer Demand Eases
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¶3. South Africa's GDP growth is expected to ease to slightly below 5% in 2006 from just above 5% this year, as consumer demand consolidates. The median forecast for 2006 is 4.9% with a range of 4.5% to 5.3%. Household consumption expenditure is forecast to slow to 5.5% next year from 6.9% in the first three quarters in 2005, 6.5% in 2004, and 3.5% in 2003. The slowing in consumer demand is corroborated by recent slowdown in real retail sales growth with September 2005 slowing to 4.7% y/y increase after 8.2% y/y rise in August and 2005's peak y/y gain of 9.3% y/y in April. With growth optimists, exports become a key determinant in attaining higher growth. For the first three quarters in 2005, exports increased 13.2% after a 2.5% gain in 2004. South African exports of bulk commodities increased by 10.6% y/y in November to a record 10.8 million tons. Those expecting lower growth fear that a possible interest rate increase will constrain consumer demand, and that government promises of increased fixed investment will not happen. General government fixed investment only grew by 4.2% y/y in the first three quarters of 2005 compared with a 12.0% gain in 2003, which slowed to 6.3% in 2004. Source: I-Net Bridge and Sunday Times, December 27.

Will the Rand Stabilize?

¶4. In 2005 the South African rand has shown less volatility than in the previous three years, prompting speculation that the rand will settle around a relatively narrow range of R6.35-6.70 per dollar for 2006. The South African rand has lost about 12 percent against the dollar in 2005 to date, its first depreciation over a calendar year since 2001 and a relatively mild move after three straight years of hefty gains. In 2002 the rand increased 40% against the dollar, in 2003 it added 28%, and in 2004 the rand increased another 18%. The rand's swings have also moderated recently. In 2005 it ranged between a high of 5.617 to the dollar, reached early in January, to a low of 6.977 in June, a difference of 136 rand cents. In 2004 its range was about 200 rand cents, in 2003 almost 300 rand cents and in 2002 it was 410 rand cents. In December 2001, when it reached 13.84 to the dollar, the currency was extremely volatile, gaining around 200 rand cents alone in the last 10 days of the year. In 1998, when the Asian currency crisis hit, the rand's range was only 200 rand cents between its high and low, illustrating that 2005 might be the beginning of a stable rand. Increased liquidity has helped, with the average daily turnover in the country's foreign exchange market has increased from $3.8 billion in the first quarter of 1998 to $13.8 billion in the third quarter 2005. Improved credit ratings and growth prospects have also helped stabilize the rand, along with increased foreign direct investment in 2005. Monetary policy has kept inflation under control, with the consumer price index measure monitored by the South African Reserve Bank within its 3% to 6% target range for 27 straight months. With commodity prices expected to remain high and growth prospects favorable, the rand should become more stable, perhaps attracting even more foreign investment. Source: Reuters, December 27.

SA's Major Banks Increase Market Share

¶5. South Africa's four largest banks continued to increase their market share, according to data from the South African Reserve Bank (SARB). In October 2005, First National Bank (FNB) has the largest market share in five of the eight categories monitored by the SARB. FNB has 47.8% of the commercial credit card market and 26.5% of the individual market. However, Standard Bank still has the largest market share in the credit card market, although they lost a large share of the commercial market during October. Nedbank has a market share of 14%, compared with ABSA's 23%, FNB's 27% and Standard Bank's 34%. ABSA dominates the mortgage market at 32%, although FNB (17%) is also providing stiff competition. ABSA also has the highest share of the overdraft market (31%), although they lost some market share from September to October. Source: Business Day, December 28.

SA, China Close to Agreement to Limit Textile Imports
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¶6. The South African government is about to conclude a voluntary restraint agreement with China to limit imports of Chinese clothing and textile products, according to Trade and Industry Deputy Minister Rob Davies. Davies said signature of an agreement on the same lines as that reached between China and the European Union (EU) earlier in 2005 was imminent. The voluntary restraint agreement between the EU and China intends to limit the growth in imports of 10 Chinese textiles and clothing products 8%-12.5% a year until the end of 2008. About four months ago the textile industry (with trade unions backing), sought government support for the imposition of WTO safeguards. WTO safeguards allow for the temporary re-imposition of quotas on Chinese clothing and textile imports if they increased to such an extent that they harmed domestic industries. However, the South African government has been reluctant to involve WTO safeguards as South Africa exports basic commodities to the Chinese market. Both labor and business have blamed the large increase in Chinese imports for the decline of the industry, which has lost an estimated 55,000 jobs since 2003. Source: Business Day, December 28.

Land Restitution Spending Increases

¶7. The Land Affairs Department spent R1.017 billion ($160 million) on land restitution in 2004-05, up from R727 million ($115 million) in 2003-04. According to its annual report, the department also spent R327 million ($52 million) on land reform programs, compared to R347 million ($55 million) spent in 2003-04. Land department programs (including administration, surveys and mapping, spatial planning and cadastral surveys which show the extent and measurement of every block of land), and land reform and restitution programs cost about R2 billion ($320 million) in 2004-05, up from R1.6 billion ($254 million) in the previous year. Source: I-Net-Bridge and Business Day, December 29.

TEITELBAUM